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In the Supreme Court of the United States

OCTOBER TERM, 1945

No. 1006

CONTINENTAL OIL COMPANY, PETITIONER

v.

THE UNITED STATES

ON PETITION FOR A WRIT OF CERTIORARI TO THE COURT OF CLAIMS

BRIEF FOR THE UNITED STATES IN OPPOSITION

OPINION BELOW

The opinion of the Court of Claims (R. 24–31) is reported in 62 F. Supp. 876.

JURISDICTION

The judgment of the court below was entered November 5, 1945. (R. 31.) On December 19, 1945, the petitioner filed a motion for a new trial which was overruled on January 7, 1946. (R. 31.) This petition for a writ of certiorari was filed March 27, 1946. (R. 49.) The jurisdiction of this Court is invoked under Section 3 (b) of the Act of February 13, 1925, as amended by the Act of May 22, 1939.

QUESTIONS PRESENTED

1. Did the Court of Claims correctly determine the taxpayer's invested capital for the year 1920?

2. Is the petitioner entitled to interest on the overpayment determined by the Court of Claims in addition to that allowed by the court under the particular circumstances involved?

STATUTES AND REGULATIONS INVOLVED

The applicable portions of the pertinent statutes and regulations are set forth in the Appendix, *infra*, pp. 13–18.

STATEMENT

The special findings of fact of the Court of Claims (R. 10–23) may be summarized as follows:

Petitioner, Continental Oil Company, is a Delaware corporation with its principal office and place of business in Ponca City, Oklahoma. (R. 10.) Prior to April 30, 1929, it was known as Marland Oil Company which by written agreement of that date acquired all of the assets of the Continental Oil Company of Maine in exchange for shares of its own capital stock. (R. 13.)

Continental Oil Company of Maine, mentioned above, was known as Mutual Oil Company prior to some time in 1925, and prior to December 22, 1921, was known as Elk Basin Consolidated Petroleum Company. (R. 13.) The taxes involved herein are those of the Elk Basin Consolidated Petroleum Company and its affiliates for the year

1920. Prior to January 6, 1920, that corporation was known as Elk Basin Petroleum Company which was organized December 11, 1916, with an authorized capital stock of 400,000 shares. On November 6, 1919, this was increased to a million shares, and again increased to three million shares on January 6, 1920. (R. 17.)

The par value of the capital stock of Elk Basin Consolidated Petroleum Company was $5 per share and the capital stock of Elk Basin Petroleum Company also had a par value of $5 per share. (R. 17.)

As of January 1, 1920, Elk Basin Petroleum Company acquired all of the outstanding capital stock of two other corporations, Grass Creek Petroleum Company and Keoughan-Hurst Drilling Company, in exchange for 600,000 shares of its own capital stock in the respective amounts of 133,333⅓ shares and 466,666⅔ shares. (R. 12.)

On March 15, 1920, Elk Basin Consolidated Petroleum Company acquired all of the outstanding capital stock of Mutual Oil Company of Maine and all the outstanding stock of each of Mutual Oil Company's three subsidiary corporations in exchange for 600,000 shares of its own stock. On March 15, 1920, and prior thereto Mutual Oil Company of Maine had as subsidiaries and owned all of the outstanding capital stock of Mutual Oil Company of Arizona, Mutual Refining and Producing Company, and Northwestern Oil Refining Company. (R. 12.)

On March 15, 1921, Elk Basin Consolidated Petroleum Company, hereinafter referred to as the taxpayer, filed its completed federal consolidated income and excess profits tax return for the calendar year 1920. That return included its own income and the income of Grass Creek Petroleum Company, Keoughan-Hurst Drilling Company, Mutual Oil Company of Maine, Mutual Oil Company of Arizona, Mutual Refining and Producing Company, and Northwestern Oil Refining Company for the entire calendar year 1920. The tax and interest shown due on the return were duly assessed and paid. (R. 11.)

The Commissioner of Internal Revenue audited the above-mentioned return and determined that it erroneously included the income of Mutual Oil Company of Maine and its three subsidiaries for the period January 1 to March 14, 1920. The Commissioner held that there were two different and separate affiliated groups of corporations; that the change in affiliation required a separate computation for the first fractional part of the year 1920; that a separate consolidated return should have been filed for the period January 1 to March 14, 1920, by the Mutual Oil Company of Maine for itself and its three subsidiaries; and that its income for that period should not have been included in the taxpayer's return. (R. 11–12.)

As a result of these adjustments, the Continental Oil Company of Maine received a 60-day let-

ter proposing to assess a deficiency. An appeal was taken to the United States Board of Tax Appeals; the case was twice before the Court of Appeals of the District of Columbia and this Court had denied certiorari. The litigation ultimately terminated in the Government's favor in 1944. No question as to that deficiency is involved in this proceeding, although both involve the same tax year. (R. 14.)

On March 9, 1925, a claim for refund was filed by the Elk Basin Company for the calendar year 1920 in the amount of $200,707.45, setting forth that the taxpayer was entitled to a refund resulting from an overstatement of taxable income and an overstatement of invested capital made by the Commissioner. (R. 15.)

Upon the examination of the refund claim filed March 9, 1925, the Commissioner of Internal Revenue determined an overpayment of tax by the Elk Basin Company in the sum of $12,779.97 and duly issued a certificate of overassessment therefor, together with a check in such amount, plus accrued interest thereon of $4,475.09. That check was rejected and returned by the Continental Oil Company of Maine to the Commissioner, together with the certificate of overassessment. The check and the certificate were subsequently cancelled and the money repaid into the Treasury of the United States. In making that determination, the Commissioner computed a consolidated net income of $1,084,800.52, and a consoli-

dated invested capital as adjusted of $7,926,731.74. The Commissioner in this determination allowed an amount of $5,726,775.95 as representing the value of the acquisitions of Grass Creek Petroleum Company, Keoughan-Hurst Drilling Company, and Mutual Oil Company of Maine and subsidiaries. (R. 15–16.)

An application was later made to reopen and reconsider the claim for refund which was granted pending final decision of the appeal to the Board of Tax Appeals, mentioned above. After the Board proceedings were concluded, the claim for refund was reconsidered and rejected in full by the Commissioner on December 13, 1941. (R. 16.)

Stock of the Elk Basin Petroleum Company and Elk Basin Consolidated Petroleum Company was traded on the New York Curb Exchange in the years 1919 and 1920. Quotations taken from the New York Times and from the Financial & Commerce Chronicle show that for the week ending January 2, 1920, 8,600 shares of Elk Basin Petroleum Company stock were sold at a low of $8½ and a high of $9 per share; that for the week ending March 19, 1920, 12,700 shares of the stock of Elk Basin Consolidated Petroleum Company were sold at a low of $10 and a high of $10¾ per share and that on March 15, 1920, an unknown number of shares were traded at a low of $9 and a high of $11¼ per share. (R. 17–18.)

During the autumn of 1919, the firm of C. H. Pforzheimer & Company, brokers and dealers in securities, was an active dealer in the stock of Elk Basin Petroleum Company, both in the capacity of broker and trader. That firm had formed a syndicate to deal in the Elk Basin stock and in November and December 1919 sold 200,000 shares at $7.50 per share. In December 1919 that firm also acquired 100,000 shares of the capital stock of Keoughan-Hurst Drilling Company at $8.50 per share. This was part of a plan whereby Elk Basin Petroleum Company was to acquire all of the outstanding capital stock of Keoughan-Hurst Drilling Company and Grass Creek Petroleum Company. (R. 21–22.)

In July 1920 Elk Basin Consolidated Petroleum Company, the taxpayer, filed its federal capital stock tax return, reporting 1,800,000 shares of capital stock outstanding with a par value of $5 per share. The Commissioner proposed an additional tax based upon an increased value for the capital stock. (R. 22.) The taxpayer replied by letter dated October 26, 1921, under oath, stating in substance that par value of its stock should be used rather than the quoted Curb market value for a number of reasons, among which was the alleged fact (R. 23)—

> that the market quotations for Elk Basin stock were not a fair criterion of its value since the block of stock exchanged for the securities of the Mutual Oil Company

> (600,000 shares) had been placed in escrow and remained so and that the block of stock exchanged for the Keoughan-Hurst stock had also been placed in escrow and that the market quotation of the Elk Basin stock was thus maintained at a higher level than would have been the case had the entire number of shares been subject to sale; * * *.

And further (R. 23)—

> that the market for the Elk Basin stock on the New York Curb was strongly supported by certain New York Curb brokers, who, by furnishing a ready and strong market for this stock, maintained its price at considerably above the value reflected by the books of the corporation.

The Commissioner thereafter accepted these statements and accepted the capital stock tax return and the value therein reported of $5 per share as correct. (R. 23.)

The Court of Claims found that the consolidated invested capital of the Elk Basin Consolidated Petroleum Company for the calendar year 1920 after giving effect to all adjustments, including the acquisitions of stock on January 1 and March 15, 1920, was in the amount of $7,926,731.74 (R. 23), and gave judgment accordingly for the petitioner in the amount of $12,156.99 with interest (R. 24).

ARGUMENT

1. The principal question is the determination of the taxpayer's invested capital for the calendar

year 1920. This depends upon the amounts to be included therein on account of the acquisitions of stock of other corporations on January 1 and March 15, 1920. The determination of invested capital under the earlier Revenue Acts based in part on the value of property paid in for stock, is no longer of any general importance. Under the last excess profits tax, which was repealed by Section 122 (a), Revenue Act of 1945, Public Law 214, 79th Cong., 1st Sess., the criterion for invested capital was the tax basis of property paid in, rather than its value. See Section 718, Internal Revenue Code (26 U. S. C. 1940 ed., Sec. 718).

The holding of the court below that the values allowed by the Commissioner of Internal Revenue in his computation, as evidenced by the certificate of overassessment which was later cancelled, represented reasonable additions to invested capital on account of the actual value of the property paid in, is in accordance with the evidence introduced in this case and with the facts as set forth in the court's findings. As the court points out, these values were based on the best evidence available. The record before this Court (R. 1–49), does not establish that the court erred in accepting these values and does not afford any basis for any other method of computation or for reversal of the court's findings.

The statute requires that the actual cash value of the property paid in be employed. The prop-

erty paid in consisted of certain corporate shares, but taxpayer's entire case here is based upon the view that it is entitled to employ the value of the stock which was issued for the property paid in. It is true that such an expedient is sometimes resorted to (Cf. *Budd International Corp.* v. *Commissioner,* 143 F. 2d 784 (C. C. A. 3d), certiorari denied, 323 U. S. 802), but here there has been no showing that it was not possible to prove the actual cash value of the property paid in. The court below assumed, without deciding, that the expedient might be resorted to here. (R. 28.)

Even on that assumption, the Court of Claims was clearly correct in rejecting the Curb Market prices alone as an appropriate method for determining value. The Court of Claims pointed out the artificiality of those prices in the peculiar setting of this case (R. 28–29), and that on another occasion the taxpayer itself had successfully urged that they were not a reliable guide.

2. The court below allowed a refund based on a computation using the same invested capital as that used by the Commissioner of Internal Revenue in the certificate of overassessment issued in 1925 and a net income of $1,087,025.43,[1] which was slightly less than that used by the Commissioner. This resulted in a refund of $12,156.99 upon which the court allowed interest at 6% per

[1] This was the amount that the parties stipulated in this proceeding as the correct net income. (R. 30.)

annum from December 16, 1921, the date of payment of the tax, to a date "not later than 30 days preceding the issuance of the refund check which plaintiff rejected, which interest was a part of the interest of $4,475.09 heretofore tendered by defendant." (R. 24.) Petitioner contends that under Section 177 (b) of the Judicial Code, as amended by Section 808 of the Revenue Act of 1936 (Appendix, *infra*), it is entitled to interest on the principal amount from the date of payment to a date preceding the date of the refund check, i. e., the check in payment of the judgment allowed by the court, by not more than 30 days. This allowance would give the petitioner interest of over 144% on an amount which was tendered to it but which it refused to accept. The court's judgment allows interest of approximately 36%, since the refund check was issued on November 14, 1927.[2] This would be the same rate of interest which the Commissioner allowed in his computation of the overpayment. Since the taxpayer had been tendered the amount which the court ultimately determined it was entitled to but refused to accept it, and since Section 177 (b), as amended, recognizes the principle that a tender stops the running of interest, we submit that there has been a substantial compliance with the statute.

[2] This date does not appear in the record in the court below but has been verified from the files of the Bureau of Internal Revenue.

CONCLUSION

The petition presents no substantial basis for certiorari; it should be denied.

Respectfully submitted.

J. HOWARD MCGRATH,
Solicitor General.

SEWALL KEY,
Acting Assistant Attorney General.

J. LOUIS MONARCH,
ELIZABETH B. DAVIS,
Special Assistants to the Attorney General.

MAY 1946.

APPENDIX

Revenue Act of 1918, c. 18, 40 Stat. 1057:

SEC. 325. (a) That as used in this title—

* * * * *

The term "tangible property" means stocks, * * *.

SEC. 326. (a) That as used in this title the term "invested capital" for any year means (except as provided in subdivisions (b) and (c) of this section);

(1) Actual cash bona fide paid in for stock or shares;

(2) Actual cash value of tangible property, other than cash, bona fide paid in for stock or shares, at the time of such payment, but in no case to exceed the par value of the original stock or shares specifically issued therefor, unless the actual cash value of such tangible property at the time paid in is shown to the satisfaction of the Commissioner to have been clearly and substantially in excess of such par value, in which case such excess shall be treated as paid-in surplus: *Provided,* That the Commissioner shall keep a record of all cases in which tangible property is included in invested capital at a value in excess of the stock or shares issued therefor, containing the name and address of each taxpayer, the business in which engaged, the amount of invested capital and net income shown by the return, the value of the tangible property at the time paid in, the par value of

the stock or shares specifically issued therefor, and the amount included under this paragraph as paid-in surplus. The Commissioner shall furnish a copy of such record and other detailed information with respect to such cases when required by resolution of either House of Congress, without regard to the restrictions contained in section 257;

(3) Paid-in or earned surplus and undivided profits; not including surplus and undivided profits earned during the year;

(4) Intangible property bona fide paid in for stock or shares prior to March 3, 1917, in an amount not exceeding (a) the actual cash value of such property at the time paid in, (b) the par value of the stock or shares issued therefor, or (c) in the aggregate 25 per centum of the par value of the total stock or shares of the corporation outstanding on March 3, 1917, whichever is lowest;

(5) Intangible property bona fide paid in for stock or shares on or after March 3, 1917, in an amount not exceeding (a) the actual cash value of such property at the time paid in, (b) the par value of the stock or shares issued therefor, or (c) in the aggregate 25 per centum of the par value of the total stock or shares of the corporation outstanding at the beginning of the taxable year, whichever is lowest; *Provided,* That in no case shall the total amount included under paragraphs (4) and (5) exceed in the aggregate 25 per centum of the par value of the total stock or shares of the corporation outstanding at the beginning of the taxable year; * * *.

Revenue Act of 1936, c. 690, 49 Stat. 1648:

SEC. 808. INTEREST ON JUDGMENTS.

Section 177 (b) of the Judicial Code, as amended, is amended to read as follows:

"(b) In any judgment of any court rendered (whether against the United States, a collector or deputy collector of internal revenue, a former collector or deputy collector, or the personal representative in case of death) for any overpayment in respect of any internal-revenue tax, interest shall be allowed at the rate of 6 per centum per annum upon the amount of the overpayment, from the date of the payment or collection thereof to a date preceding the date of the refund check by not more than thirty days, such date to be determined by the Commissioner of Internal Revenue. The Commissioner is hereby authorized to tender by check payment of any such judgment, with interest as herein provided, at any time after such judgment becomes final, whether or not a claim for such payment has been duly filed, and such tender shall stop the running of interest, whether or not such refund check is accepted by the judgment creditor." (28 U. S. C. 1940 ed., Sec. 284.)

Internal Revenue Code:

SEC. 3771. INTEREST ON OVERPAYMENTS.

(a) *Rate.*—Interest shall be allowed and paid upon any overpayment in respect of any internal revenue tax at the rate of 6 per centum per annum.

(b) *Period.*—Such interest shall be allowed and paid as follows:

(1) *Credits.*—In the case of a credit, from the date of the overpayment to the

due date of the amount against which the credit is taken, but if the amount against which the credit is taken is an additional assessment of a tax imposed by the Revenue Act of 1921, 42 Stat. 227, or any subsequent Revenue Act, then to the date of the assessment of that amount.

(2) *Refunds.*—In the case of a refund, from the date of the overpayment to a date preceding the date of the refund check by not more than thirty days, such date to be determined by the Commissioner, whether or not such refund check is accepted by the taxpayer after tender of such check to the taxpayer. The acceptance of such check shall be without prejudice to any right of the taxpayer to claim any additional overpayment and interest thereon.

* * * * *

(26 U. S. C. 1940 ed., Sec. 3771.)

Treasury Regulations 45 (1920 ed.):

ART. 862. [as amended by T. D. 4102, VI–2 Cum. Bull. 291–292 (1927)] *Purchase of stock.*—Where a corporation either directly or indirectly, as for example through a trustee, purchases its own stock, either for the purpose of retiring or of holding it in the treasury or for other purposes, the cost of such purchase to an amount equal to the capital paid in to the company for such stock must be deducted from the aggregate invested capital from the date of such purchase. Where any such purchase is made within the first 60 days of the taxable year, any sum paid in excess of the above amount will be deemed to have been made from earnings or profits accumulated during pre-

ceding taxable years; but any such excess paid in such a purchase which occurs during the remainder of the taxable year will be deemed to have been made from the earnings or profits accumulated between the close of the preceding taxable year and the date of payment, to the extent of such earnings or profits. See article 857. The full amount derived in cash or its equivalent from the resale of such stock may be included in invested capital from the date of such resale. See article 542.

ART. 864. *Affiliated corporations: invested capital.*—The invested capital of affiliated corporations, as defined in section 240 (b) of the statute and article 633, for the taxable year is the invested capital of the entire group treated as one unit operated under a common control. As a first step in the computation a consolidated balance sheet should be prepared in accordance with standard accounting practices, which will reflect the actual assets and liabilities of the affiliated group. In preparing such a balance sheet all intercompany items, such as intercompany notes and accounts receivable and payable, should be eliminated from the assets and the liabilities, respectively, and proper adjustments should be made in respect of intercompany profits or losses reflected in inventories which at the beginning or end of the taxable year contain merchandise exchanged between the corporations included in the affiliated group at prices above or below cost to the producing or original owner corporation. Such consolidated balance sheet will then show (a) the capital stock of the parent or principal company in the hands of the